

1 *Approved March 4, 2003*

2
3 **VIRGINIA TOBACCO INDEMNIFICATION AND**
4 **COMMUNITY REVITALIZATION COMMISSION**

5 701 East Franklin Street
6 10th Floor
7 Richmond, Virginia 23219
8

9 **FULL COMMISSION MEETING**
10 John Marshall Hotel – Marshall Room
11 Thursday, February 6, 2003
12 6:00 p.m.
13

14 **Attendees**

15 Senator Charles R. Hawkins, Chairman
16 Senator William C. Wampler, Jr.
17 Senator Phillip P. Puckett
18 Senator Frank M. Ruff
19 Michael J. Schewel
20 Secretary of Commerce and Trade
21 John Bennett
22 Secretary of Finance
23 Gary D. Walker
24 Isiah G. Hopkins
25 Fred M. Fields
26 Buddy Mayhew
27 John M. Stallard
28 J. T. Taylor
29 Thomas Arthur
30 Jack Hite
31 H. Ronnie Montgomery
32 Claude Owen, Jr.
33 Mary Sue Terry
34 Tucker C. Watkins
35 J. Carlton Courter
36 Commissioner of Agriculture
37 Clarence D. Bryant
38

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COMMISSION STAFF

Carthan F. Currin, III
 Executive Director
 Tim Pfohl
 Grants Manager
 Mary Cabell Sherrod
 Manager of Communications and Committee Operations
 Stephanie S. Wass
 Director of Finance

ATTORNEY GENERAL'S OFFICE

Frank Ferguson
 Anne Marie Cushmac
 Stephanie Hamlett

SENATOR HAWKINS: All right, let's reconvene.
 Carthan, would you call the role?

MR. CURRIN: Mr. Arthur.

MR. ARUTHUR: Here.

MR. CURRIN: Secretary Bennett?

SECRETARY BENNETT: Here.

MR. CURRIN: Delegate Byron?

DELEGATE BYRON: No response.

MR. CURRIN: Mr. C. D. Bryant?

MR. BRYANT: Here.

MR. CURRIN: Mr. Courter?

MR. COURTER: Here.

MR. CURRIN: Delegate Dudley?

DELEGATE DUDLEY: No response.

MR. CURRIN: Mr. Fields?

MR. FIELDS: Here.

MR. CURRIN: Mr. Hite?

MR. HITE: Here.

MR. CURRIN: Delegate Hogan?

1 DELEGATE HOGAN: No response.
2 MR. CURRIN: Mr. Hopkins?
3 MR. HOPKINS: Here.
4 MR. CURRIN: Delegate Johnson?
5 DELEGATE JOHNSON: No response.
6 MR. CURRIN: Delegate Kilgore?
7 DELEGATE KILGORE: No response.
8 MR. CURRIN: Mr. Leigh?
9 MR. LEIGH: No response.
10 MR. CURRIN: Mr. Montgomery?
11 MR. MONTGOMERY: Here.
12 MR. CURRIN: Owen?
13 MR. OWEN: Here.
14 MR. CURRIN: Senator Puckett?
15 SENATOR PUCKETT: Here.
16 MR. CURRIN: Senator RUFF?
17 SENATOR RUFF: Here.
18 MR. CURRIN: Secretary Schewel?
19 SECRETARY SCHEWEL: Here.
20 MR. CURRIN: Mr. Stallard?
21 MR. STALLARD: Here.
22 MR. CURRIN: Mr. Taylor?
23 MR. TAYLOR: Here.
24 MR. CURRIN: MS. TERRY?
25 MS. TERRY: Here.
26 MR. CURRIN: Mr. Thompson?
27 MR. THOMPSON: No response.
28 MR. CURRIN: Mr. Walker?
29 MR. WALKER: Here.
30 MR. CURRIN: Senator Wampler?
31 SENATOR WAMPLER: Here.
32 MR. CURRIN: Mr. Watkins?
33 MR. WATKINS: Here.
34 MR. CURRIN: Mr. West?
35 MR. WEST: No response.
36 MR. CURRIN: Mr. Williams?
37 MR. WILLIAMS: No response.
38 MR. CURRIN: Delegate Wright?

1 DELEGATE WRIGHT: No response.

2 MR. CURRIN: Mr. Chairman.

3 SENATOR HAWKINS: Here. Welcome. Many of the
4 members of the House of Delegates aren't here. They're working on
5 a budget and they might join us later. Before we get started I want to
6 call on Senator Ruff.

7 SENATOR RUFF: Mr. Chairman, with your permission
8 I'd like to give you sort of an introduction. We have a fellow who has
9 agreed to help the Hartland Group as they try to market themselves
10 and Lee Cobb. Lee if you'd stand up so they all recognize your face.
11 He has a wealth of experience working in the Lynchburg area and
12 before that in the Portsmouth area and he's going to make a big
13 difference for us and I want you all to know him and get to know him.

14 SENATOR HAWKINS: He's done an outstanding job.
15 Before we get started we've got some new members on the
16 Commission so I thought we'd go around the table and have
17 everybody introduce themselves and who you are.

18 MR. MAYHEW: I'm Buddy Mayhew from Pittsylvania
19 County and I'm Chairman of the Concerned Friends of Tobacco and
20 I'm also a tobacco producer.

21 MR. HITE: I'm Jack Hite from Southside, Mecklenburg
22 County.

23 MR. WATKINS: You all know me. Tucker Watkins
24 from Halifax County and I own a tobacco farm and work for Senator
25 Allen.

26 MR. STALLARD: I'm John Stallard from Scott County,
27 Southwest, Virginia and I'm a tobacco farmer.

28 MR. MONTGOMERY: I'm Ronnie Montgomery from
29 Lee County and I am a tobacco farmer and lawyer.

30 MR. TAYLOR: I'm JT Taylor from Clarkesville and
31 I'm retired.

32 MR. ARTHUR: Tom Arthur from Pittsylvania County.
33 I'm a citizen member and own a farm in Pittsylvania County.

34 MR. BRYANT: I'm C.D. Bryant from Pittsylvania
35 County, tobacco producer.

36 MR. WALKER: I'm Gary Walker from Charlotte
37 County, Chairman of the Board of Supervisors.

38 SENATOR RUFF: I'm Frank Ruff.

1 SENATOR WAMPLER: I'm William Wampler, a
2 member of the Senate.

3 SENATOR HAWKINS: Charles Hawkins, member of
4 the Senate.

5 MR. CURRIN: I'm Carthan Currin and I work for
6 everybody, I work for the Governor of Virginia.

7 SECRETARY SCHEWEL: I'm Mike Schewel,
8 Secretary of Commerce and Trade.

9 MR. HOPKINS: I'm Isaiah Hopkins, Lunenburg
10 County.

11 SENATOR PUCKETT: I'm Phillip Puckett, member of
12 the Senate.

13 MR. OWEN: I'm Claude Owen from Danville, retired.

14 SECRETARY BENNETT: I'm John Bennett, I wish I
15 was retired. I'm the Secretary of Finance.

16 MR. COURTER: I'm Carlton Courter, Virginia
17 Commissioner of Agriculture.

18 MR. FIELDS: Fred Fields, tobacco farmer and an
19 educator from Lee County.

20 MS. TERRY: I'm Mary Sue Terry.

21 SENATOR HAWKINS: Before we get started, one of
22 our Commission members, Mr. Banner from Russell County had a
23 heart attack and is hospitalized. He should be in our prayers and I
24 understand he's doing better and will be home tomorrow. Hopefully
25 he'll be back to the Commission soon.

26 MR. CURRIN: Mr. Chairman, I would like to introduce
27 Tim Phohl who's our Grants Manager and he's new on board.

28 SENATOR HAWKINS: We have a fairly complicated
29 agenda. Before we get started I think I need to make a few comments
30 which is my nature. We're beginning to get to a stage in this
31 Commission that's been long in coming and we need to make sure
32 that we're focused on what we need to be doing. This body is charged
33 in trying to change the economic fortunes of an entire population that
34 encompasses a pretty large section of Virginia and runs the gamut
35 from the coal fields all the way across. Mostly encompasses the
36 tobacco industry but also includes the coal fields, textiles, furniture,
37 all those jobs that have historically given us a certain amount of
38 wealth and prosperity that we no longer can count on.

1 We have been given a charge by the General Assembly
2 of Virginia to invest these monies to improve the opportunities of all
3 the people in our areas. There's been comments made over the last
4 several months about various areas achieving more from the front end
5 of this discussion and probably that may be so particularly Danville
6 and Pittsylvania County because they started a joint effort early on to
7 put in place a basic infrastructure and improvement with the money
8 for a five year plan. The thing we need to understand is that as areas
9 come up with plans that are viable, it's our obligation to weigh them
10 on their merits and for us to make sure that they complete their project
11 regardless of their location. We have gone through this process in
12 trying to identify several market pieces that we hold up as to what we
13 have accomplished as a Commission. I'm very pleased to say we
14 have several.

15 The first being the basic infrastructure of a new high
16 speed cable on 58 and referred to as the E58 project. This will give us
17 the next generation of telecommunications access and for a brief
18 period of time we'll have an advantage over every community in this
19 country in this part of the world because we'll have the next
20 generation of high speed connectors that will be at an affordable price
21 for all of our citizens. Virginia Tech has been a major player in
22 developing the program for us and they're working on a plan that they
23 will probably unveil at the next meeting. At that time, it should be
24 ready we hope. We have a committee in place that's looking at that.
25 My idea is to put it in place as quickly as possible, the basic backbone
26 down Route 58 using a combination of everything we can find to put
27 it in place. This starts the outreach from that by giving the design to
28 tie all the communities themselves to the backbone, eventually tying
29 in Tech which gives access to the research component and the
30 research triangle in North Carolina and that will give us an advantage
31 that will really pay off long term, I believe. This cable is also
32 designed to hook up with the Atlantic Cable, which gives us access to
33 the international cable. It's a unique concept that's driven by the
34 Tobacco Commission and to challenge the Tobacco Commission to
35 try to improve our communities. The speed on the leg of this cable is
36 going to be driven by how fast we can contract this out and the plans
37 we have in place and no county should be left out of the basic
38 background in the next couple of years I hope.

1 Aside from that, we have developed in the City of
2 Danville and Pittsylvania County, a concept which is called the
3 institute, which is another child of this Commission. The Institute is
4 not a higher education center. It is a research component. If an area
5 plans to develop economically, you must have one of three
6 components; interstate highway we do not have, access to a four-year
7 university research component we do not have, international airport
8 we do not have. This institute gives us access to a four-year research
9 institute in the City of Danville that will benefit not the City of
10 Danville and not Pittsylvania County but the entire region. It will
11 implore research components with Virginia Tech tied into the
12 backbone to allow this development not only bio-informatics with
13 Virginia Tech for farmers but research components working with
14 NASA that will develop the next generation of components that we're
15 using. The VIR Racetrack is looking to us and the airport in Danville
16 and the Institute for Research. Also surrounding communities
17 bringing in other aspects of research. We start from the basics and
18 build from there. That's another paramount piece that we developed.

19 What I want to emphasize to all members of this
20 Commission, the monies we're charged with has to go to the benefit
21 of the entire population regardless of what they decide to do. It's also
22 been brought to my attention that many of the smaller counties are
23 somewhat concerned about not getting projects online. We have
24 never turned down a project for lack of money. Projects that are
25 taking place will be funded with sufficient money to do the job and
26 money left over for investment. We've got to do something to help
27 our small counties become part of the overall economic stability and
28 to do that, we're going to recommend and hope to have in place very
29 soon, economic development people in Southside and Southwest
30 Virginia working with smaller counties to develop a long range plan
31 that we can start implementing and funding; be it micro-business and
32 all the way through. The thing you must remember because we're
33 talking about securitization and a long-range plan and that is every
34 county and every citizen in this entire region is tied together by the
35 same thread and need. We have lost population and our demographics
36 are all basically the same, we're older and we're getting poorer
37 because our students are leaving our areas and going to college and
38 not coming back because the jobs are not here and we've got to

1 reverse that and it's our challenge to do it.

2 The ideas we come up with and approaches we take are
3 going to return in economic stability of an entire group of people that
4 deserve no less. So as we get into these discussions in the next couple
5 of days, I want to emphasize as strongly as I can, this Commission is
6 not driven by desires to have one county over another or the political
7 reasons or anything else. We don't have time to bother with that sort
8 of thing. We're here to do that which is in the best interest of
9 everyone we represent and we will not bring any of that baggage with
10 us. We need regional projects that have regional importance and also
11 help counties with basic infrastructure that they need.

12 Also, over the years we have developed a set of standards
13 that we call the formulary that are tilted towards tobacco and areas
14 based on quota and based on jobs and based on the impact of tobacco.
15 Those that are driven by an understanding that these counties would
16 be affected greatest because the loss of tobacco. Also, over the years
17 we understood fully that the pure formulary that we had in place tilted
18 the amounts of money that large counties and large populations with
19 the tobacco quota.

20 This Commission initiated several approaches to balance
21 out the field. We took six million dollars off the top, which was given
22 to the community colleges in our area regardless of location. Then we
23 started setting aside monies for special projects that go into a special
24 pool right off the top that would be accessible to every community
25 within our area that had a need for a special project to go into place
26 and also deal closings. Deal closing monies have been spent across
27 the entire spectrum if there was a need and it was justified by the
28 amount of money that was generated in jobs and standards that were
29 met. We have complimented the Governor's opportunity fund more
30 times than we can count and brought in business.

31 Ladies and gentlemen, our charge is to figure out how we
32 can mesh together with the great diversity that is rural Virginia under
33 one tent to approach one goal that is for the betterment of the people
34 that we represent. As we get into the securitization conversation, I
35 want to emphasize as strongly as I possibly can, securitization gives
36 us protection but it also gives us unique challenges because the flow
37 of money that we're used to from the Master Settlement Agreement
38 will not be there. We're going to have to manage better by making

1 sure that we do some things that matter. We have a long-range plan
2 that we'll discuss in a minute and we need to understand the
3 components of that are education, development, jobs, business
4 opportunity, infrastructure improvement and everyone's involved.

5 We have also entered into with the leadership of Senator
6 Ruff, an education component not only to help people because our
7 population is undereducated through no fault of their own. At a time
8 in our history education was not an important factor to get a job. You
9 could go to the mill or go to the farm and it's gone. We've got to give
10 people access to GEDs so they can go to community colleges and
11 prepare themselves for the economy. We've put money aside for
12 scholarships for teachers and nurses and that's two disciplines that we
13 badly need but we want them to stay back in these areas after they're
14 trained and not leave. We want to put that in place and encourage
15 that. That's an investment in our future.

16 We must understand today that this Commission will
17 change yearly and the nature of it. Our foundation has to be one that
18 transcends decades and decades so these monies are managed by a
19 corporation who manages the economic future and this is a heavy
20 responsibility and we need to make sure we understand that charge.
21 It's also been brought to my attention that there were people that were
22 not brought into the mix early on in the City of Martinsville. The City
23 of Martinsville did not have a tobacco quota or warehouses. When
24 they needed money, the Tobacco Commission came up with funds to
25 fund things for Martinsville and will continue to do that because they
26 are part of our community. Other smaller counties and allocations
27 were used up based on the formulary and when they needed money
28 for deal closings, we came to their need because deal closings were
29 there. We've invested heavily in some of these counties because of
30 jobs coming in and the demand was there. To step back from
31 opportunities in Franklin County or Pittsylvania County or Halifax
32 County or Mecklenburg County simply because someone is afraid
33 they're getting a little bit bigger bite at the apple does not serve the
34 good of this Commission. We need to keep our eye focused on one
35 thing and our job has one purpose and one purpose only, to make the
36 lives of the people in our area better and give them better
37 opportunities.

38 Having said that, we have before you a new executive

1 summary of the committee assignments. Initially the committees
2 from this Commission came about because of our need. We set up
3 committees because we needed to get things done so we put
4 committees in place. It was quickly realized that for this Commission
5 to function, there had to be a focus on different disciplines in our
6 areas. We're breaking down the different committees and we're
7 doing away with some and consolidating others and making sure to
8 try to get an equal distribution of participation through these
9 committee and adding two that we did not have before. We're putting
10 in place, not only the two technology committees dealing with the E58
11 project or dealing with any telecommunications questions that come
12 up or any other technology questions to make sure that we have in
13 place funding to deal with that when questions come up regarding
14 locations.

15 The next thing we're going to try to deal with is the new
16 agribusiness subcommittee dealing with the tobacco areas with the
17 bio-informatics and agribusiness questions come up. Not to
18 concentrate exclusively on tobacco today but other crops. That was
19 formerly the Tobacco Committee but that's been changed to the
20 Agribusiness Committee and that will be charged with a tremendous
21 responsibility to help our farmers transition themselves from tobacco
22 dependence locations to much more varied locations using Tech and
23 using the components of the Institute for Research and Development,
24 the next generation of profit for our farmers.

25 If you go through trying to balance these regions and we
26 have an understanding of the individual desires as well as more
27 background information to bring into this. These Committees will be
28 the ones that will make recommendations to the full Commission. So
29 I would strongly suggest that individuals serving on these various
30 committees become very aware of the subject areas and also the
31 monies needed so when we get into long range planning you can start
32 putting money aside for infrastructure, special projects, deal closings
33 and telecommunication pieces and various other components.

34 The only one that's different than the rest is E58. This is
35 comprised of Commission members and non-Commission members.
36 We found two individuals that had the time and the dedication to put
37 into the development of this and also their personal resources into this
38 and that has made a real difference. I think we need to understand

1 that this is a different thrust to make sure that we have access to
2 markets.

3 Having said that Carthan, we'll get on with the business.
4 Is there any comments or questions? Again I apologize for taking so
5 much time. Yes, sir.

6 MR. CURRIN: Next is a presentation by Dr. Tom
7 Morris who is President of Emory and Henry College and he co-
8 chaired the long range planning taskforce and finalize their report
9 several months ago. Charley Majors also co-chaired this taskforce
10 from Danville and he's not here tonight but Dr. Morris will give us a
11 summary. The Executive Committee met this evening and
12 unanimously passed a recommendation for approval to the full
13 Commission.

14 SENATOR HAWKINS: We have to approve the
15 minutes from the October 30, 2002 meeting. Is there a motion to
16 approve the minutes of the October 30, 2002 meeting? (So moved
17 and seconded) All those in favor say aye (ayes) opposed (no
18 response).

19 DR. MORRIS: I will just briefly report on the long-
20 range plan. Charley Majors isn't here tonight, he's in Florida. As
21 Carthan said, we started our work last summer and we had a number
22 of various extensive sessions where we got into both a broad base and
23 long term view of the problems and challenges that are facing the
24 regions, the tobacco regions. I would just say to you that we focused
25 on the legislation and the first goal of the Commission which was
26 indemnification of the tobacco farmers and that was a major piece of
27 the long-term plan. Also another feature of this that I would highlight
28 for you is the suggestion that in fact a model for a non-profit
29 foundation be used as you go forth with the securitization of the
30 money. That there would be a number of program officers, two or
31 three program officers that would be part of the Commission with
32 expertise in areas that we identified. Specifically they would be
33 charged with getting the proposals and receiving and analyzing the
34 proposals and for presenting recommendations for proposals to the
35 Commission, for overseeing awards of pending proposals and
36 providing for accountability for the Commission's funded projects.
37 We felt that was a very important component of the long-range plan in
38 terms of setting up a process and structure.

1 Another item I would call your attention to was the
2 suggestion that there be a general funding policies. Among those, as
3 part of the report, were that funds should not be used to supplement
4 other local, state, or federal funds and that's an important principal.
5 Funds should be leveraged to the greatest extent feasible, funding
6 from other public and private sources. Funding should not be used to
7 fund annual operating costs beyond start up costs. There was a great
8 deal of discussion about that. That funding should not be used to fund
9 endowments. Most foundations do not give money to other people
10 that endow programs. Finally, before any funding can be approved,
11 an application must be submitted in accordance with guidelines and
12 deadlines established by the Commission and be reviewed by the
13 appropriate program directors of the Commission. Those were the
14 important components of the policy and structure of the long-range
15 plan.

16 I don't know what else I can say beyond what Senator
17 Hawkins said about the categories we set out for funding allocations
18 and that there was a consensus there needed to be some infrastructure.
19 Two infrastructure categories; one on telecommunications and one on
20 human infrastructure to compliment the other two categories; deal
21 closings and job creation and the regional economic development.
22 Those were the four categories that were set up and indemnification in
23 terms of funding allocations.

24 I could say more about the long-range plan but you had it
25 for a couple of months and I know you've looked at it. Maybe I
26 should stop here and see if there's any questions.

27 SENATOR HAWKINS: I want to thank you for the
28 work you all did. I know a great deal of effort went into all this and I
29 know you all tried to address the new entities and all the work that
30 you did and all the meetings and speakers that were present. Has
31 everyone had an opportunity to review the long-range plan? Any
32 discussion among the members or questions?

33 MR. WATKINS: I think I've already mentioned this
34 earlier and I don't want to do it again but there is one question that I
35 have. Certainly after this discussion, are we going to pass this?

36 SENATOR HAWKINS: I would certainly like to pass it.
37 We need to have a procedure or report in place for long range
38 planning.

1 MR. WATKINS: I do have a question, I'm looking at
2 fiscal year '03 appropriations for different categories. I know you told
3 the communities it's 25 million in this year Southside, is that is
4 subject to this or is that money already there?

5 SENATOR HAWKINS: This year's allocations are
6 based on the old formula. We're not securitized as yet but we're
7 looking at a long-range plan based on the assumption that we're going
8 to securitize.

9 MR. WATKINS: So, that answers that part '04. My
10 only suggestion for this is that under the indemnification piece, once
11 the 50 percent of the excess earnings in a given year be distributed
12 proportionately for other funds. Then it could drop down to the
13 regional development area. Once that indemnification is paid out,
14 those funds go back down into the categories that, from what we have
15 now are going to be cut significantly.

16 SENATOR HAWKINS: Although the indemnification
17 piece was based on loss of tobacco –

18 MR. WATKINS: I understand that.

19 SENATOR HAWKINS: We may have future
20 obligations that we need to –

21 MR. WATKINS: - I understand that so when that
22 happens and rather than drop it down into everybody, you would drop
23 it down all the way.

24 DR. MORRIS: The assumption was that the
25 Commission at some point in time would define personnel.

26 SENATOR HAWKINS: That's a discussion we won't
27 get into, how much money we hold in reserve and at what point do we
28 say that?

29 MR. WATKINS: But you're going to divide it, it's
30 going to be divided equally, why not drop it down all the way?

31 SENATOR HAWKINS: At the time if that is the –

32 MR. WATKINS: Then I'd like to make a motion to
33 amend this plan and make that happen.

34 SENATOR HAWKINS: I don't quite understand that.
35 Do you want to take the money now that's set aside for
36 indemnification?

37 MR. WATKINS: No, I don't want to touch any money
38 at all. It says in the bottom part of the indemnification, it says 50

1 percent of excess earnings in a given year may be distributed
2 proportionately to other funds. Rather than do that proportionately to
3 the other funds, just say that that money would fall in there so the
4 communities that are currently doing long term economic planning,
5 long term indemnification. If you pass the long-range plan it wouldn't
6 make sense now, it doesn't make sense to have to go back and change
7 the policy.

8 SENATOR HAWKINS: What's the advantage of
9 lumping that or taking that or putting it there?

10 MR. WATKINS: The advantage of putting it there rather
11 than the other place?

12 SENATOR HAWKINS: Yes.

13 MR. WATKINS: So there wouldn't be as much impact
14 on those communities that would be cut. In this plan you're cutting
15 money that goes into the economic development piece for hard money
16 in half. Once that economic impact hits, indemnification dollars
17 stopping, that's going to happen.

18 SENATOR HAWKINS: No, that's not. I think there
19 may be some misunderstanding. The allocation formula that we have
20 in place and if we cut back on the money, a portion of the money is
21 still there so we're going to know what they're getting. But even if
22 you put the money into various areas that we're talking about, and
23 give everyone access based on jobs and based on all the things we're
24 talking about, and it gives everybody access to the same monies.

25 MR. WATKINS: It does but it doesn't put the money in
26 those areas affected most by losing those dollars that are going into
27 the communities. The formula you put together is based on the
28 economic impact and loss of tobacco jobs.

29 SENATOR HAWKINS: Well, the thing that's lacking in
30 this and needs to be understood is not just indemnification money. So
31 I think what you want to do is protect the communities by increasing
32 the money that goes to the allocation portion.

33 MR. WATKINS: Exactly. When that impact hits and all
34 the money is not all indemnification –

35 SENATOR HAWKINS: - The indemnification piece is
36 personal receipts of money that had nothing to do with the accounting
37 itself.

38 MR. WATKINS: It doesn't have anything to do with

1 when those monies are going to quit coming into the community.

2 SENATOR HAWKINS: We're going to offset those
3 monies.

4 SENATOR WAMPLER: Mr. Chairman, tonight we
5 have two cabinet secretaries from Governor Warner's administration
6 with us and there's no other group that I know of or no other political
7 subdivision or Commission that has that kind of leadership at the table
8 given this time of year. I think it shows the commitment of Governor
9 Warner that he recognizes the impact of what we're about to do
10 accepting the long-range plan and hopefully get on with the business
11 of securitizing the proceeds. I know as we went through the long
12 range planning process there were a lot of things as one member of
13 the Commission, I disagreed with some and I agreed with some and
14 there was a lot of balancing and we were able to craft a long range
15 plan to try to address what we believe were the most important things
16 for Southside and Southwest were indemnification. Number one an
17 economic development and infrastructure and all the things we talked
18 about.

19 I hear the discussion and I think it was with regard to the
20 plan. We wanted a general blueprint or a guideline, if you will, a
21 guideline. Yes, we think these are goals. I didn't agree with all the
22 seven points within those goals but at least it gave us a document that
23 we could communicate to the executive and say these are what our
24 goals are. Tucker, I might agree with you that we need to apply more
25 dollars in certain areas but I don't think this is the document that
26 drives that decision. This is the document that tells the executive that
27 we've set out goals and we're ready to proceed with the financial
28 transaction. I would say that's a healthy debate to have but I'm not
29 sure that for purposes of receiving this report it is the appropriate time
30 to have that discussion. That's just one opinion, Mr. Chairman and
31 members of the Commission.

32 MR. WATKINS: I think we should set a time to have
33 that discussion.

34 SENATOR HAWKINS: We can have additional
35 discussion on that. Any other discussion? This is a good night, it's
36 snowing outside and there's nothing you can do and we can be here
37 for a while. So anyone that has anything to add to the conversation
38 let's go ahead and get it.

1 SECRETARY SCHEWEL: In response to the question, I
2 think it's going to be six years or so depending on quota before we get
3 out of indemnification.

4 MR. WATKINS: Depending on whether you use this
5 number or another?

6 SECRETARY SCHEWEL: I think the ultimate question
7 raised is pretty far out, a lot of years to think about it.

8 SENATOR HAWKINS: The secretary is right, the only
9 thing that will, I don't think you can change the demand of that, there
10 are several buyout programs with many changes and we're not there
11 yet. Any comments, any other comments? We have the long-range
12 plan before us recommended by the Executive Committee. Is there a
13 motion?

14 MS. TERRY: Mr. Chairman, are we getting ready to
15 vote on it?

16 SENATOR HAWKINS: We need to do that.

17 MS. TERRY: I certainly don't want to, but I think I need
18 to register a concern. We seem to have had very good discussion
19 about one of the concerns I had. I'm a new member of the
20 Commission but I hear a language and conversation, both public and
21 private that remind me of conversations I heard on the floor of the
22 General Assembly representing Patrick County when Hampton Roads
23 and Northern Virginia would say we need to put our money where we
24 can create the most jobs. We put our money where the taxpayer
25 money comes from in the first instance and we need to put our money
26 where the most people are. We fought and struggled Mr. Chairman,
27 we worked together across party lines and we fought and struggled to
28 try to get people to see there needed to be some kind of basic floor.
29 Back in those days it was paving roads, having indoor toilets. I feel
30 like this Commission now, dealing with Southside and Southwest,
31 they are the haves and have-nots. I feel like we need to be more
32 explicit at some point Mr. Chairman about what are going to be our
33 concerns now and in terms of not sitting back and particularly in terms
34 of waiting for people to apply for special funding. You indicated
35 earlier we would be helping localities develop leadership and jobs. I
36 asked several weeks ago for information concerning county-by-county
37 and city-by-city what people had gotten through allocations,
38 education, special education or through special projects. I was just

1 handed that or got a hold to that and I wish I had it before this meeting
2 and I asked someone to go out and make copies so that everyone here
3 would have it.

4 On one hand Mr. Chairman I would agree with you that
5 we need to go after improving counties. We have localities that have
6 not improved, much less ever having a prospect of improving. I just
7 want to read off some of the disparity and have us all ponder about
8 our commitment to the entire region. You said in your opening
9 remarks not just individual counties. I'm reading this and not by way
10 of criticism but I think it provides a baseline from which we can go
11 forward with special projects, in education, economic development.
12 We need to keep in mind and keep these figures before us as we seek
13 for equity across our region.

14 In the Southside area and Southwest Virginia, and I'll
15 just read Southside, per capita expenditures for Amelia County the
16 total funding per capita is \$34. Appomattox County - \$6, the City of
17 Bedford - \$3, Brunswick County - \$283, Buckingham County - \$3,
18 Campbell County - \$68, Charlotte County - \$124, Cumberland
19 County - \$12, Dinwiddie County - \$70, Franklin County - \$36,
20 Greenville County - \$40, Halifax - \$219, Henry County - \$58,
21 Lunenburg County - \$158, Mecklenburg - \$166, Nottoway County -
22 \$30, Patrick - \$53, Pittsylvania County - \$179, Prince Edward - \$21,
23 Sussex - \$15, Danville City - \$118, Emporia City - \$11, Martinsville
24 City - \$35. Now, I'm going to read from the list of localities that have
25 gotten no grants at all from this Tobacco Commission apart from
26 whatever allocation there might be through the allotment. Amelia has
27 not gotten any grant, Appomattox has not, Buckingham County has
28 not, Cumberland County has not, Dinwiddie County has not,
29 Nottoway County has not, Bedford City has not and then there are
30 counties that have gotten very little and then some of the counties that
31 have had the greatest allotment Mr. Chairman, have been the ones that
32 have gotten the greatest special projects grants. I'm not saying that's
33 improper, I'm just saying we need and I think we all benefit by being
34 stewards of all our counties because we know what it's like being in
35 the General Assembly where we're out voted and everyone thinks
36 they're giving us a free ride and where everybody has told us that we
37 got to put the money where the most jobs are. I had one legislator tell
38 me years ago, people don't have to live here. If we really make a

1 commitment and my concern Mr. Chairman is that I don't see
2 reflected in the long range plan a value system or equity statement that
3 would help us go forward in ensuring that no county and no city is left
4 behind.

5 SENATOR HAWKINS: I think I can build on that MS.
6 TERRY. The discussion between Mr. Watkins and yourself are two
7 different things. Tucker is talking about the formulary and enhancing
8 the formulary and you're talking about the opposite. The Commission
9 over the years has recognized what you have brought out and realizing
10 that the formularies we have in place was helpful. Bedford City
11 doesn't have a plant and neither does Martinsville. We have set aside
12 in special projects and that was built into the long-range plan how
13 these special projects would work and their development. The only
14 flaw I see in your argument is that when I hear it, counties like
15 Franklin or Pittsylvania or the City of Danville should be stagnant
16 while everyone else tries to catch up and we can't do that. We need to
17 encourage all of our communities to develop at a speed which they
18 can accomplish their goals. The City of Danville has dealt with the
19 loss of jobs and population due to a change in the economy and we do
20 not have the luxury of waiting. We have to act as rapidly as possible.
21 Pittsylvania County and the City of Danville with their population and
22 in cooperation came up with a long-range plan they wanted to fund.
23 That long-range plan developed a few years out. I'll repeat myself, no
24 county has been turned down for funds that had a legitimate program
25 online. You also have to realize that if you look at some of these
26 small counties competing in the overall market because of lack of
27 experience and economic development. That's the reason we're going
28 to hire people to develop programs in these counties to help people
29 compete for the overall jobs out there and the businesses that are out
30 there.

31 The only thing I can say to you MS. TERRY is that
32 looking at the overall thrust of what we're trying to accomplish, if you
33 take out populations that are largely tobacco dependent and the City
34 of Danville is one because jobs have been there for generations. The
35 allocations coming from those areas were based on those jobs that
36 were impacted. I represent Pittsylvania County but I was the first to
37 realize that in order to bring some stability to the overall system, we
38 needed to put money into different areas quickly. My county suffered

1 by my decision because I realized it was fair that the college money,
2 special projects money, education money and I wanted to continue
3 building this to make sure that everybody would have access to these
4 monies when monies were needed. I can assure you that in Franklin
5 County or Henry County or Patrick they had an opportunity or a need
6 for 350,000, I want to make sure the money is there to close the deal.
7 I don't want to sit back and say we spent it all last week, sorry, come
8 back later. We're not going to do that.

9 MS. TERRY: Mr. Chairman, I agree with you there.
10 Eighty-five percent of what you said, I heard you say at the outset
11 we're not going to have the revenue stream we had before and we'll
12 have to spend our money wisely. So I can't assume that if every
13 county that were in need got up to speed and had the leadership shown
14 in Danville and Pittsylvania County that there would be money there
15 to fund all the projects. But what are we going to do or what would
16 be our principals for determining how we allocate limited funding?
17 What would be our baseline? I don't really know what that is, I don't
18 know where it ought to be. All I know is that one of the reasons our
19 state is in the shape it is is because of folks in other parts of the state
20 who wrote us off because they were going faster and they were in the
21 pipeline and they had access to the means to get things that we didn't.
22 I would just suggest that we not do to some of our counties what has
23 been done to our whole region over the years.

24 SENATOR HAWKINS: I can understand your point.
25 The State of Virginia is the only state I know of that has allowed
26 access to this amount of money to economic development. Also, our
27 economic situation is somewhat of our own making because we were
28 comfortable. For generations we have been very comfortable being
29 dependent on tobacco and furniture and that's who we were and we
30 were comfortable doing this. When things started to change, we
31 weren't as anxious to change with it. As we lost our youth and our
32 own population, we liked the security of what we were doing and
33 didn't want to change. I can understand it. I've reached the age in
34 life I see changes take place now and I'm not so sure that's right but
35 that's the nature of the beast. We did not sit back and say just because
36 certain things took place some place else we're going to have to do
37 something. But now we have to look at this whole thing on a regional
38 thrust. I think E58 is a good example. It's not so much the low

1 hanging fruit but I can assure you that if we don't pull the fruit off
2 when it's ripe, it'll rot and have no benefits to anyone except for the
3 crows. We've got to look at this differently.

4 Tucker's point I disagree with him. I think the bottom
5 line is there needs to be greater access to all of our counties and
6 money available for economic development. I think the formulary
7 gave stability to those counties that were counting on those monies.
8 We need to get beyond that and that's an understanding I think we
9 need to have. We cannot put the formulary in place to guarantee a
10 county money unless they have something to offer for it. We cannot
11 put money there, there must be something we can do. We can hire
12 economic development people, we can do things that need to be done
13 to work with rural counties and make sure they have access to these
14 funds. But there again, rural prosperity is not defined. A lot of people
15 can tell me what rural prosperity is like farming, small houses, not
16 factories, not high rises, not condominiums. Floyd County is one that
17 likes who they are. I'm not real sure you can put all this together but
18 people in Floyd County want to live in a rural environment and work
19 in the City or work in Lynchburg and drive back and forth. But they
20 work places where the jobs are. If we build something in the City of
21 Lawrenceville or Stuart that benefits counties outside of the Carroll
22 area or Grayson or Floyd, people will travel in and out of the county
23 and benefit the county while people that work in these other cities
24 who live where they want to live, build nice homes and pay more real
25 estate taxes. What I'm saying is that we've got to look at the big
26 picture and to do that, we need creative thinking and we need to have
27 people who are open minded and understand the whole specter of
28 what we're trying to do. I'm willing to do that and I'm willing to
29 understand the different viewpoints.

30 MR. ARTHUR: Has that motion been seconded?

31 MR. WATKINS: I question because all these figures
32 match and I couldn't figure exactly why they did. I went back and
33 looked at tobacco and that's all money that went to the community
34 colleges. When you look at this chart, you really have to take
35 Brunswick, Campbell, Henry \$1.7 million out of Pittsylvania because
36 those were not really set, those were education funds that went to the
37 community colleges.

38 SENATOR HAWKINS: Let's get back on track.

1 MR. WATKINS: You can't take half of the money away
2 from Brunswick County.

3 SENATOR HAWKINS: The subject matter is the
4 adoption of the report. Let's take up the report and get back into the
5 agenda. It's been moved, is there a second?

6 MR. MAYHEW: Second.

7 MR. HITE: I've listened to Tucker and could I have the
8 information –

9 SENATOR HAWKINS: I'm going to refer this in just a
10 second. It's been moved and seconded that the overall plan be
11 adopted. Any discussions?

12 MR. ARTHUR: Is there a motion that it be adopted or is
13 there a motion that it be amended?

14 SENATOR HAWKINS: The motion was to receive the
15 report.

16 MR. ARTHUR: Has that been seconded?

17 SENATOR HAWKINS: The motion is to receive the
18 report, is there a second? Discussion? All in favor (aye) opposed (no
19 response). The report is adopted. Now, Tucker, getting back to this.
20 This is the first time I've seen this, this is a breakdown of monies
21 allocated in the formulary and also on the type of special projects. It's
22 being distributed. The problem I have distributing it tonight is that
23 it's not complete. The indemnification money is not included in this.
24 This gives a good understanding of what we're doing. This was not
25 on the agenda. All education components need to be looked at
26 separately. Special projects money may, Pittsylvania County put all
27 their money, it went into. But we got to mix apples and apples and
28 oranges and oranges. This will be, we'll get to the discussion of this.
29 I think this underscores the need to have access monies for other
30 projects that come online rather than going back to the strict
31 formulary. Alright, I know you all are sitting there very patiently and
32 I apologize and this is probably one of those pieces that is probably
33 not running in the highest gear. Mrs. Wagner is the Treasurer of
34 Virginia and she has undertaken a lot of this work on securitization
35 and what she has to say in her presentation is very enlightening and
36 will help us understand the complexities of the securitization issues.

37 SENATOR WAMPLER: Before Mrs. Wagner speaks, it
38 will be appropriate to thank Dr. Morris and Mr. Majors for their work

1 (applause).

2 MRS. WAGNER: Mr. Chairman and Committee
3 members, we have been working on getting the Commission in a
4 position to go forward with this securitization. As you can recall, the
5 actual securitization is done by a corporation created by the staff. The
6 corporation will consist of five appointed members and the Treasurer
7 is an ex officio member. Governor Warner has appointed the
8 corporation members and I'm passing out a sheet with their names on
9 it. This was rather complicated and the lawyers developed two
10 volumes of books so far in doing it. Once this organization is formed
11 and we accomplish it, there are ongoing tasks that this program is
12 responsible for. Just to give you a glimpse of it, we prepared a list of
13 exactly what is entailed. At the very end of it, is a flowchart that
14 shows how the money works. Sharing this information with you, lets
15 you get a feel for what's involved and what is to be accomplished.
16 The actual securitization is worked out by a team of professionals and
17 I'll take a minute to introduce some of them to you and some of them
18 you already know. Morgan Stanley has been involved well before I
19 ever thought of it. We have James Vergara, Rocky Query, Rob
20 Larkins. They're from Morgan Stanley. Then we have David
21 Richardson and Arthur Anderson from McGuire Woods, the Bond
22 attorneys. The underwriters have hired counsel Chuck Shimer from
23 Troutman Sanders. The Commonwealth has financial advisors called
24 Public Resources Advisory Group who has worked on this
25 transaction. The Public Resources Advisory Group has done some
26 investigative work and their sole job is to look after the welfare of the
27 Commonwealth and they're not paid on the basis of whether or not we
28 sell or how much we sell. They are paid on an hourly basis. They've
29 been working on this the past few years. They also give advice and
30 information with regard to what they know and how they feel.

31 Tonight we appreciate you coming and we really do but
32 the thing we need from you this evening is because the transaction is
33 in a position to move forward but we can't move forward until the
34 Commission lets us know how to do this transaction. By adopting the
35 long range plan telling us how you plan to spend money and that's a
36 huge step forward because in doing that we can start putting things in
37 clarification and start figuring out how we finance it based on your
38 directions. Tonight we'll ask you to decide three things; the first is

1 taxable or tax exempt and the reason that's relevant is that you can
2 only use tax exempt proceeds for certain things. Essentially capital
3 projects, building buildings, structures. Then there's things you want
4 to do such as indemnification, cost of administration, scholarships,
5 training, economic development in the form of advertising. Those are
6 the types of things called working capital expenses. They can be done
7 with the tax-exempt dollars or leave the 2003 money aside and not
8 securitize. That's the first question, how much is taxable and how
9 much is tax exempt. The second question is what percentage are you
10 going to securitize? We can securitize all of it or do half of it or 80
11 percent. It's whatever the Commission wants in order to accomplish
12 your goals. To the extent that you chose not to securitize any of it,
13 there's free money you can use for working capital or whatever you
14 decide. Then the final thing we need your advice on is determining
15 the bond. Whether you want a 25-year bond or 30 year bond. We've
16 asked Morgan Stanley to put together a presentation and lay the
17 groundwork for those questions and then McGuire Woods will take
18 questions and then hopefully we can get to you. Please don't leave
19 the room so we can move forward on this. Be glad to answer any
20 questions.

21 SENATOR HAWKINS: Questions?

22 MR. TAYLOR: On the 80/20 that would leave 20
23 percent working capital funds. Would that be enough to fund our
24 group or the expenses?

25 MRS. WAGNER: On the long range plan what
26 Stephanie did is took the long range plan and put dollars on it and
27 several numbers and based on that, the 80/20 would work. The
28 question is how much flexibility you want. If ultimately you decided
29 you wanted to use half of it every year, then no, we couldn't do it but
30 if you did the allocation with the long-range plan, you could.

31 MR. TAYLOR: And the education funds, you could use
32 them?

33 MRS. WAGNER: Under this scenario, yes.

34 MR. QUERY: My name is Rocky Query and what we
35 want to do is provide a few specifics to help you answer the three
36 questions that the Treasurer laid out. We passed around a short
37 presentation just to give you some information so you could work
38 with it and if you have any questions, we will be glad to answer those.

1 We've got a few slides here we'd like to show you. You've got a hard
2 copy of the visual slide there. I don't want to repeat the information
3 the Treasurer covered. Our primary goal is sort of laid out on page
4 three and we can jump right into it here. That was to essentially make
5 this securitization structure work for your long term plan. That really
6 was the framework for providing the analysis but frankly without the
7 long-term plan, it was very difficult to come up with a financial plan
8 that would in any way be responsive for basing any practical realities
9 about how securitization could increase the effectiveness of the
10 Commission's spending goals. The program goals are laid out as they
11 are in the long-range plan. The second step was to really look at that
12 by the base categories that the treasurer described in terms of working
13 capital and operating and spending that would be done in each of the
14 categories. There was an effort by Stephanie, in particular, to look at
15 all the grants that had been made and all the spending that had been
16 done in the program areas over time. In order to come up with a
17 realistic allocation of the typical purposes if there is such a thing, of
18 the spending that would happen in each of those categories. So what
19 we actually did was come up with a proportion of capital needs and
20 working capital needs to serve as a good framework for what we
21 expect the spending to be like in the future according to those two
22 basic categories. What we did next is on page four, was to build on
23 that framework and make sure that –

24 SECRETARY SCHEWEL: Mike, let me interrupt one
25 second. The question you asked about is there going to be enough
26 money for the 80/20, just to be sure we're all straight here. When you
27 look at this chart on page three, this is saying that for 2003, you would
28 have to generate a basis of 39.9 million dollars of taxable, non-tax
29 exempt monies to pay for working capital needs in '03. \$25.8 million
30 in '04 and \$24 million in '05 and \$23.8 in '06. So measuring the flow
31 of the funds against the plan and that's really the number we got to get
32 at. So if the financial plan we come up with delivered that amount of
33 money available for working capital purposes, then it will work based
34 on the long-range plan.

35 MR. QUERY: I think everyone understands the basic
36 reason for wanting to make these distinctions between working capital
37 and capital purposes and it's really driven as we summarize on page
38 four by the basic factor that we do the securitization. If we finance on

1 a tax-exempt basis, we only do that effectively for capital purposes
2 and working capital purposes on a taxable basis. The other
3 consideration, the – taxable basis as McGuire Woods can provide you
4 any amount of detail on, it's essentially to make sure that whatever
5 those funds are being spent on, it's done in such a way as to make sure
6 that there is no return of funds to the Commission that would result in
7 you needing to treat this as a taxable rather than tax exempt. In order
8 to do that, McGuire Woods has helped us with a very helpful
9 definition of what you might look to as qualified for capital
10 expenditures and what you might look for to qualify as working
11 capital expenditures. I think it's relatively straightforward. The areas
12 where it might get a little gray would be areas such as education and
13 training expenses of one kind or another when you're dealing with
14 human capital issues. For the sake of argument, we would assume
15 those costs are basically working capital to keep you out of a gray
16 area. I'm going to turn it over to James but we looked at three
17 specific areas that we ran to give you a sense of what the trade offs are
18 as we look at more capital debt, or less, as we look at shares of the
19 MSA which you may not securitize and as you look at this question of
20 the actual turbo bonds.

21 MR. VERGARA: My name is James Vergara and I've
22 been working with Rocky and Morgan Stanley on the
23 Commonwealth's benefits since 1999. Right now I'd like to spend a
24 few moments to talk to you about the issues that Treasurer Wagner
25 and Rocky talked about and recommended structures for
26 securitization. If you turn to page seven and the first issue is that of
27 the tax status of the bond and what percentage is tax-exempt versus
28 taxable. Based upon the long-range plan as it was shown on page
29 three, you could fund all of this spending which is roughly \$54
30 million after 2006 with that breakdown of working capital versus
31 capital on a 100 percent tax exempt basis but there is a little
32 flexibility. Tax-exempt increases your flexibility for working capital
33 expenditures in the event you need funds for additional
34 indemnification payments for non-qualifying loans. If you look at a
35 table comparison of what structure that is, that is 100 percent tax-
36 exempt, it looks like it's 100 percent taxable, 80 percent tax exempt,
37 20 percent taxable. You can see part of the \$682 million for the entire
38 life of the tax exemption versus \$668.9. The interest costs is the

1 difference between the two; 27 basis points by issuing 20 percent on
2 the taxable basis. Then the number you're interested in is \$578.5
3 million for 100 percent tax exempt versus \$561 million. The
4 difference what you're paying for in that \$17.5 million is the second
5 to last line, 113.7 taxable capital which would add to your flexibility
6 to go forward. Both of these structures assume a 25-year plan, which
7 we'll talk about later.

8 MR. QUERY: I'd like to add one point to that as well.
9 We made a clear distinction between working capital and capital. On
10 the tax-exempt bonds, for working capital purposes your taxable
11 bonds and then we're saying it could be both with 100 percent tax
12 exemption issue. Those are not inconsistent and it's complex but
13 they're not inconsistent. We're able to fund a certain amount of
14 working capital needs over time through a combination of funds that
15 are already available that are not subject to the tax exempt restriction
16 and we're able to do that because of a certain amount of funds are
17 freed up each year that can be spent.

18 SENATOR HAWKINS: What is the reason behind
19 doing both, why do you want taxable and nontaxable. What can you
20 do with the taxable monies as opposed to the nontaxable. Non-taxed
21 money as I understand it, is fairly limited in the way that it can be
22 invested.

23 MR. QUERY: Tax-exempt monies would be limited in
24 terms of reinvestment and limited in terms of purposes that you can
25 spend.

26 SENATOR HAWKINS: Taxable monies would be
27 included in what categories?

28 MR. QUERY: Taxable monies could essentially be spent
29 on anything both capital purposes and working capital purposes.

30 SENATOR HAWKINS: And indemnification is what?

31 MR. QUERY: Indemnification, we consider that
32 working capital.

33 SENATOR HAWKINS: That's something, we'd have to
34 consider that as part of the tax, thank you sir.

35 MR. QUERY: We want to be sure that you're clear. If
36 funds were according to that plan, a hundred percent taxable basis,
37 then clearly the 20 percent is issued taxable. You simply got more
38 flexibility and an opportunity to accommodate things that have not

1 been thought of or discussed yet that might fall into a working capital
2 category.

3 MRS. WASS: One hundred percent tax exempt, that's
4 assuming that the percentage you have used in the past for working
5 capital versus capital is the same percentage in the future and that's
6 why it can be done.

7 MRS. WAGNER: If we had a crystal ball we could say
8 the plan is perfect and we never want to change it and we could have
9 done 100 percent tax exempt. I'm worried that you want flexibility.
10 If you don't have flexibility you might say why did you mess this up.
11 The second part is that even if the percentages are the same, there are
12 less dollars. Once you securitize the cash flow significantly changes
13 and you'll see that in the plan. In '03 it doesn't really affect you but
14 in '04 and '05, you're going to go from \$75 million to \$52 million of
15 usable cash. You may want that flexibility.

16 MR. VERGARA: How much of the MSA revenue is
17 securitized? On the previous page the assumption of 100 percent of
18 your money after 2004 are sold for a lump sum. That's at the end of
19 the financing. Here we're going to look at securitizing half of the
20 money. With the other half you've got flowing to you as it does
21 currently, it's decreased the cost of your securitization by half but it
22 also increases your annual exposure to the risk that you're trying to
23 divest yourself of by securitization. In the table below, 100 percent
24 tax exempt securitization of half your MSA allocation, the 25-year
25 plan you have \$340 million par amount with \$289 million net bond
26 proceeds. If you look at that closer, turn to page nine and I'd like to
27 show you the difference between spending in the plan based on
28 securitization of a hundred percent versus spending that you may have
29 available assuming that you securitize half of your allocation and
30 continue to receive payments on an ongoing basis for the other half
31 unsecuritized. The bar on this graph reflects spending \$79 million in
32 '04 and going forward. What we've done is that the bar represents
33 half of the spending in the plan based on half of the securitization and
34 then spending unsecured amount on an annual basis which is roughly
35 out of the endowment, then you can spend roughly 30 or 40 million
36 unsecured monies.

37 SENATOR HAWKINS: That's what the assumption that
38 the MSA will stay viable through the out years and that's a pretty

1 good assumption.

2 MR. VERGARA: But it does assume that payments
3 come in as projected by the global insight prepared forecast but if you
4 believe that payment is going to come in as scheduled, you derive a
5 benefit from leaving a portion unsecured.

6 MR. WATKINS: Is there a certain percentage that
7 should not be securitized or do you have a number there?

8 SENATOR HAWKINS: The discussions we had when
9 we met about securitization is that we talked about 50 percent and we
10 also talked about the risk factor. The last time we had a discussion
11 it's my understanding that we pretty much, we agreed on 100 percent
12 securitization. I may be wrong but I think that's correct.

13 SECRETARY SCHEWEL: This 50 percent
14 securitization, the reason I was pushing that is not because I think it's
15 right or wrong but I think we need to see that because as we look at
16 that yellow line, it's clear that when you securitize a hundred percent,
17 80/20, you're substantially reducing the annual cash flow over cash
18 flow that you would have if the payments stay the same. The cash
19 flow that you would have if you only securitize 50 percent. If you say
20 I think there is a risk of payment or slow payment or whatever the risk
21 might be, if you have to take the risk on the other half. When you see
22 that, you have to recognize that when you do a hundred percent we're
23 going to be receiving less cash.

24 MR. WATKINS: I think the first time they came in and
25 talked about securitization it was said you could not securitize all of
26 the cash flow, you only securitize 80 percent or 90 percent.

27 SENATOR HAWKINS: We were talking about taxable
28 and non-taxable.

29 MR. VERGARA: If you turn to page 10, on this page
30 you're looking at a 25-year versus 30-year financial plan and laying
31 out the differences and extending the final maturity. You can see if
32 you're selling a longer term of payment but it refers to the residual
33 you expect to see after the bonds mature. In the table you can see the
34 difference 25-year and 30-year financing. Again we're assuming an
35 80/20-split tax exempt and taxable. The 25-year is 668.9 and the 30-
36 year plan is 705.6. The 30-year is longer of course and it comes out
37 as a higher interest rate and roughly 20 basis points more than the 25-
38 year financing. It results in \$29 million greater proceeds that you get

1 today.

2 SECRETARY SCHEWEL: That means the cash flow
3 between the years 25 and 30 are discounted more.

4 SECRETARY BENNETT: If you look at that \$29
5 million, you have in the additional MSA payments \$88 million and
6 you get about a third for the last five years.

7 MR. VERGARA: \$29 million. Another point with the
8 full turbo feature, future payments coming in on schedule, 25 year
9 financing is fully paid off in 2017 and the 30 year financing the bonds
10 are paid off in 18. So you're selling a five-year additional bond
11 assuming the payments come in as scheduled, you're only extending
12 the maturity by one year.

13 SENATOR HAWKINS: The turbo has an advantage by
14 creating a larger cash flow.

15 SENATOR WAMPLER: I'm not an expert but this is
16 the fifth time I've heard this presentation. The important point is that
17 the instrument retires in 2017.

18 SECRETARY BENNETT: That's the point. As
19 payments come in as projected and you pay the outstanding bonds off
20 sooner, you get the residual sooner, depending on the MSA payments
21 coming in as projected. With your cash flow there's very little margin
22 for error year to year.

23 SECRETARY SCHEWEL: If you take and assume the
24 turbo feature which assumes the MSA payment will be made, if in
25 fact the MSA payment is made why not securitize - . Assuming and
26 counting on the turbo feature, it seems to me inconsistent with the risk
27 factor you made when you did the securitization.

28 SENATOR WAMPLER: I'd say Mr. Secretary, you're
29 right, however, this is what I've been lead to believe that the market
30 has to have in the pricing of the instrument.

31 SECRETARY BENNETT: The market is expecting the
32 turbo feature -

33 SENATOR WAMPLER: - If we restructured it any other
34 way, it's not going to be received in the market so that's kind of
35 where it is.

36 SENATOR HAWKINS: The assumption is as I
37 understand it, that after 25 years or 30 then if everything is in place
38 we can pick up just like we were.

1 MR. VERGARA: Once the bond is paid off.

2 MR. OWEN: What's the interest rate on tax-exempt
3 versus taxable?

4 MR. VERGARA: The tax-exempt on the 25-year is 6.85
5 percent yield and on the 30 percent it's 7 percent. On the taxable
6 bond we assume 325 spread over treasury which is about 6.25 percent
7 in both cases.

8 MR. QUERY: The taxable rate is lower simply because
9 we put it up front at the lowest yield at the end of the yield curve.

10 MR. WATKINS: If you use this turbo, is the risk gone
11 after 2017?

12 SENATOR HAWKINS: My understanding Tucker the
13 risk is still, we're talking about securitizing now. Once that's
14 completed the payments pick back up.

15 SENATOR WAMPLER: The marriage goes into year
16 2017. You can pretty well count on that assuming the payments are
17 made. If your question is what happens at the end of that, assuming
18 those payments were made, that transaction goes. We pick the MSA
19 payments back up in year 15 and thereafter.

20 SECRETARY SCHEWEL: The way I think it is and you
21 all correct me if I'm wrong, the MSA payments are greater than the
22 amount of money necessary to amortize the debt. We're taking that
23 excess amount, if in fact we receive it, and using it to prepay the debt.
24 When the debt is prepaid, then we start receiving all the MSA
25 payments ourselves.

26 MR. WATKINS: In 2017 we don't have the risk?

27 MR. QUERY: Well, what we're talking about and I
28 think the important point is that you're talking the risk spectrum and
29 talking about extending the term of the bond and the result of
30 extending the term of the bond obviously it brings you extra costs
31 associated with securitizing a large portion. Also it extends the period
32 of time over which you defer the risk associated with the MSA
33 payments.

34 SENATOR WAMPLER: Mr. Chairman, I move and this
35 is probably stretching it a bit, give out the numbers and get by our
36 experts and we're trying to transfer the risks for two reasons. Number
37 one is the domestic consumption or protracted litigation. The other is
38 what I would call the we're transferring the risk of political

1 consideration. What makes this Commission think that five years
2 down the road a future governor and/or General Assembly just might
3 grab all the cash. I would say this is one person's observation that if
4 we leave half of the proceeds on the table, they just might say they
5 didn't need it. Secretary Bennett will tell you that the Appropriation
6 Act will override about anything around it but it makes a very, very
7 tall and wide firewall to go over and get these dollars. That's why I
8 think leaving any money on the table that we don't securitize leaves a
9 pretty good target. That's why I think we ought to securitize 100
10 percent but also the flexibility of something close to 80/20 or
11 whatever Madam Treasurer thinks will give us that flexibility at her
12 discretion and I would support that. Whatever she thinks we need to
13 do what's best in the long term.

14 SENATOR PUCKETT: Mr. Chairman, I just started
15 looking at the next page. Again, the stand on what Senator Wampler
16 just said. States all over the country are doing the same thing and I've
17 only seen this for the second time but I don't want to leave anything
18 on the table. Somebody else is going to make the decision 17 years
19 down the road because I'm not going to be here. I would like to be
20 able to say I've done everything I could to keep this money and use it
21 for what we're charged to do and I'd also support what Senator
22 Wampler said, 100 percent.

23 MR. LARKINS: Mr. Chairman –

24 SENATOR HAWKINS: Mr. Larkins.

25 MR. LARKINS: Mr. Chairman and the Commission, as
26 you think evaluating the market it's really important background
27 information for you to consider as you evaluate policy consideration
28 on securitization. Over the past couple of years, we've seen a
29 significant widening spread in the rate of premiums that are paid on
30 tobacco bonds over general marketing and municipal issues. That
31 spread has widened out quite a bit over the past couple of years to the
32 point where the prevailing rate is about two percent over an ordinary
33 municipal bond. So the prevailing rates in the market are somewhere
34 around seven percent. The reason for that is very simple because
35 unlike ordinary taxes and bonds or revenue from an enterprise or a tax
36 base, there's really nothing municipal about these bonds. It's all paid
37 from the same industry and therefore investors are looking at the same
38 ultimate credit and we are seeing signs of saturation. During the past

1 year, several states as has been mentioned, with budget deficits and
2 we've listed them here such as Wisconsin, Rhode Island, New Jersey,
3 Puerto Rico, Washington and California. A point of reference, most
4 of these deals have 40-year maturity except for Wisconsin and
5 Washington. So I think if you're looking at the 25 and 30, certainly
6 it's in the norm for this market. There is a lot of competition out there
7 for the same investor base. Looking to a few months ahead the fiscal
8 pressures around the nation remain quite large. New Jersey is on the
9 calendar for \$1.8 billion later this month, New York State is
10 contemplating an aggregate of approximately \$4.8 billion. The first
11 piece to come in March and the second piece in March. California is
12 coming back in June to the Market for \$2 billion. These are just the
13 announced issues. There are several legislative proposals around the
14 country being considered as well as a few California counties that are
15 trying to grasp with their own budget deficit. So I think we are seeing
16 signs of capacity and pressure on the prevailing interest rates. We feel
17 comfortable with the assumptions used in providing the presentation
18 here tonight but it's a very, very volatile market.

19 SECRETARY SCHEWEL: At some point, does the
20 supply get overwhelmed for a while and then the market gets better or
21 what?

22 MR. LARKINS: Well, there's only so much capacity, so
23 for California, with the second issue, there's no more. They're done
24 and there is no more bonds. What you have by charter and by SEC
25 regulations is limits on concentration. It will take some time for them
26 to grow their asset base where the amount of tobacco bonds is now
27 back up to an allowable percentage or where in the ordinary course of
28 events in our market, those bonds will trickle on out into the retail
29 market but there's always a question of the level of saturation like
30 California did.

31 MR. OWEN: Is there a change in creditworthiness?

32 MR. LARKINS: I think certainly the overall dynamics
33 affecting the industry, price wars, impact on profitability. You may
34 have seen in the paper today RCR was suspending sponsorship of the
35 Winston Cup Series and relinquishing its sponsorship opportunity.
36 Plus they're feeling that much profit pressure to give up that
37 advertising opportunity. So there is a separate price pressure going on
38 in the industry. Price pressure put on by the lower cost manufacturers,

1 the MSA payments and you also have widespread state cigarette tax
2 concerns and the Commonwealth is considering that. On the
3 California tax, you have California adding \$1.50 a pack tax. So I
4 think investors are concerned about the underlying dynamics. In our
5 view, operating fund analysis of all this litigation as we see it is a key
6 risk to the industry. We have an outline schedule and we're here
7 tonight at your meeting and your session ends in February with
8 potential bond pricing and final sizing in March and it certainly would
9 be important to avoid traffic jams in New York and the other issues
10 coming so the transaction could conceivably be closed by the end of
11 March.

12 SENATOR HAWKINS: Just for your information, I
13 think we should be aware of the fact that once this process starts, we
14 assume an obligation of a fairly large sum of money to pay to have
15 this process start.

16 MRS. WAGNER: In your packet I think I listed the
17 expenses. Most of the expenses are things we have to pay up front.
18 Some of these things we have to pay in advance and I think that's in
19 your packet. Certain things we have to advance. For some reason if
20 this deal should break up and not happen, somebody has to pay the
21 costs. Unfortunately, the Department of Treasury doesn't have the
22 money to pay those costs and John won't give it to me.

23 SECRETARY BENNETT: It's your nickel as I said
24 earlier.

25 MRS. WAGNER: One of the things we're asking for
26 tonight is a commitment that you will stand behind the deal to pay
27 those expenses. Frankly, the only reason this deal wouldn't go
28 forward once you approved it and that would be if the market were to
29 change so quickly that Carthan and the Chairman or the Department
30 of Treasury decided it wasn't a good idea to go with that time and that
31 could be any number of major things that could happen but hopefully
32 that won't happen.

33 SENATOR HAWKINS: It's my understanding
34 Carthan's salary can be deducted.

35 MR. WATKINS: If we go forward, we can indemnify
36 his salary against that happening.

37 SECRETARY SCHEWEL: Mr. Chairman, I realize it's
38 hard to say, but how deteriorated would the market have to get before

1 we might say we're not willing to discount that much?

2 MRS. WAGNER: I don't know the answer to that. If
3 the rates go down 50 basis points, that probably would not be enough,
4 if it went to 12 percent, you'd tell me to stop the deal and I would
5 think you would. It's something we'd have to confer with our
6 advisors on.

7 SENATOR HAWKINS: Are we obligated for the entire
8 program whether it's completed or not?

9 MRS. WAGNER: You're just obligated to the point that
10 whatever expenses we had submitted, if this transaction goes forward,
11 the cost of doing it is greater than the \$650,000. Those are sort of the
12 walk away expenses. If we stop tonight, it would be a lot less. If we
13 stop next week, it's going to be more than zero so it depends how far
14 along we get.

15 SENATOR HAWKINS: That's a discussion we need to
16 be all aware of.

17 MRS. WAGNER: Well, that's something that we're
18 going to cover and you have to be aware of that. There are a lot of
19 things I had zero control over. Things could happen and require us to
20 pull the transaction and I don't think that's going to happen but I feel
21 you all need to have a real good understanding of what we're doing
22 and that really requires hearing from the financial advisor. The Public
23 Resources Group is here. The Public Resources Advisory Group has
24 done a securitization in South Carolina a couple of years ago and they
25 just completed the California securitization. And the President of
26 Public Resources Advisory Group is here, Billy Cobbs and I've asked
27 him to talk to you about the transactions in the market because when
28 you pull the trigger to do this, I want you all to understand so we can
29 be on the same page. Senator Wampler, as much as you want me to
30 make the decision, I'm not making it, you all make it. Now, I'd like
31 for those of you that don't know, I'd like to introduce Billy Cobbs.

32 MR. COBBS: Thank you for inviting me this evening
33 and I hope that this will be informative for you, I just want to make
34 sure that you all understand what we're talking about doing here. You
35 have to understand that there's some risk involved. First, let me say
36 that you all make the policy decision and I can only provide you with
37 information. One piece of information you need to understand is that
38 the risk is not totally passed off. I want you to understand that in the

1 first place, after the full turbo and payments would be made and as
2 you'll see from the handout I'm going to give you, interest rates are
3 much higher in the back end than the front end. There's greater risk at
4 the back end of the transaction.

5 SENATOR HAWKINS: So the advantage of the turbo,
6 if you pay it earlier and you eliminate some of those high interest rates
7 the last years?

8 MR. COBBS: That's one reason to have a shorter
9 maturity and the other thing is you're already, in the global insight.
10 They already have a 2.5 percent decline built in. So there's a lot of
11 risk but to me the major risk is if there were a large payment or credit
12 tax and all of a sudden companies went into bankruptcy
13 simultaneously and they put all the MSA payments on the same credit
14 standing. That to me, and I think that's unlikely because a class
15 action suit would take a long time. But if that was stopped and there's
16 also the chance they would be made to pay and if they'd be made to
17 pay ahead of all the others because it's necessary to do business. If
18 they stopped paying you, then you can bring suit on the Medicare
19 which was stopped, I mean the MSA. So please don't think there is
20 no risk left. I just wanted to make sure I said that.

21 MR. OWEN: Just to characterize it, are you speaking
22 solely of the risk that we won't resume getting the MSA payments or
23 the risk that we might have to give some of the money back? We
24 have taken the risk when we sold it.

25 MR. COBBS: I think the biggest risk you're taking and
26 you want to be protected against is as if simply all payments stopped
27 and you would have all the money up front. I think that's the biggest
28 risk you would have.

29 MR. WATKINS: Then in the short term, you wouldn't
30 be able to affect the turbo and the bonds would go longer.

31 MR. COBBS: I do have several handouts that I want to
32 pass out. I mentioned before the interest rates are going up. There's
33 two handouts and the first one, as I said before, the further you go out
34 on the maturity curve the higher the interest rate is. If you look on
35 this one, that's got all the numbers on it, you will see that the maturity
36 and along with the maturity you'll see versus the yield. There's a
37 direct correlation between the higher yield and you expect that.. But
38 here this curve is much more upwards sloping than it is in the regular.

1 This shows the risk in the longer term. The investor thinks there is
2 less likelihood to get paid out than the 40-year bond. On the 40 year
3 than on the 30 or 25 year bond. So you pay more.

4 SECRETARY SCHEWEL: When you issue the bonds,
5 are they short term or long term?

6 MR. COBBS: No, you have serial bonds normally in the
7 early years and then you have several charges going out, like
8 California was the most recent one. Those are term bonds. There's
9 one in 21 and that really did very well because it had an expected
10 average life of about 3.5 years. That's because of the turbo. You see
11 that at the bottom of the page. It says maturity 21 and it should be
12 expected average life, expected average life is 3 years and that was 2.5
13 times. In 33 with the expected average life of under 10 years, it had
14 655 and that was very slow and we struggled on that. We got it done
15 but it was a struggle. Then you go after 39 and you go out to seven
16 percent. If you look at the normal yield chart, it would not be 45 basis
17 points they call it. From 655 to 7 in just six years and that's because
18 people perceive more risk the further you go out. That's the risk. The
19 longer their held, the investors, taxable investors see much greater risk
20 and they analyze the risk and do their own stress test and they want
21 the bonds as short as possible. They want a five-year or short
22 expected average life so that will give you a sense. Then here in the
23 color chart, you can see and I guess that's November, 2001 and this is
24 the spread on the longest-term bond and Triple A and that's the
25 highest tax-exempt bond. These spreads have been widening and
26 that's what I mentioned before and Morgan Stanley mentioned that
27 there is only one asset class and if you pass that class, you get
28 saturated. So, as you go out, people demand more and more. Then
29 following up on that, and if we go out a little longer. Without taking
30 into account the California issue in January of \$3 billion, we're
31 showing about \$13 billion between now and maybe the end of
32 September. We don't know now and we think they should go sooner
33 rather than later. Another reason I say that, let's say you wait and the
34 spread is some 200 basis points and you come down to a hundred and
35 New York City sold but at the same time, we're seeing record deficits
36 in the federal budget and in all markets there's supply and demand.
37 As more bonds come, it's going to drive up the interest rate and it's
38 already happening. The taxable market is backing up and it may not

1 pull us along totally in sync but we have not improved as much as the
2 taxable market. Let's say the spread improves, the market backs up
3 by a hundred basis points then you're at the same place in terms of
4 interest rates, the very same place.

5 SENATOR HAWKINS: In your reference to the
6 marketplace, is there any foreign market?

7 MR. COBBS: That's the taxable market and that's more
8 expensive. They take all the risk they want to in that market. We
9 have in this market, maybe we get 20 years or 10 years, 10 year
10 preferred but it's much more difficult to sell a 10 year fixed rate in the
11 Euro dollar market. I think it would be very difficult to sell. On that
12 other page we handed out, it shows a calendar. New Jersey next week
13 and they're suppose to and decide in the next couple of weeks. I think
14 we're probably next up. We need to go to the rating agencies and
15 although essentially the first New York City issue they basically been
16 the same and South Carolina was the first turbo. There hasn't been a
17 lot of innovation but still the rating agency is going to take their own
18 sweet time if we have taxable. So we would like to know. I think
19 we're all set to go to the lawyers and the bankers ourselves and we've
20 got the documents and like to get on the calendar. We'd like to set out
21 our own schedule like a week in March if nobody comes in there on
22 top of us. So New York has got, and they got a budget deficit of
23 about \$2 billion and that's when they're planning to sell some bonds.
24 They're going to try to come up with some enhancement and the
25 enhancement they're talking about is a moral obligation. It's not
26 going to be what you have on the mortgage taxes and it's not equal to
27 the deficit. The reserve on the \$2 billion issue. So it's not going to be
28 enough to make the revenue bonds. They hope to be able to get a
29 different asset class so that they can improve but they're still going to
30 have tobacco. California's coming in with another \$2.5 billion to help
31 their budget deficit problems and that's going to close maybe in June
32 and then the second trouche in the fall. So, again, we would
33 encourage you that the best thing to do is go ahead if you are rather
34 than later if you all want to proceed.

35 The last thing I want to say is what kind of haircut you
36 are going to take? You got more flexibility with the taxable and you
37 don't really know what the investments going to be over the next 20,
38 25 or 30 years.

1 SENATOR HAWKINS: Can you tell us what the
2 percentage is going to be on the taxable and nontaxable? Your
3 recommendation would be what?

4 MR. COBBS: The right-hand column shows what you
5 would get over the next 25 years with the securitization discounted for
6 borrowing the cost of about five percent. The left-hand column is a
7 hundred percent, securitization 25 years maturity, 949 and your
8 haircut is 238, \$238 million. The second column shows the 80/20, a
9 100 percent securitization. Your haircut there is 255 and taxable is
10 more expensive. If you do 50 percent securitization, which there was
11 some discussion and you go a 100 percent tax exempt, 25 years
12 obviously it's lower. Then the fourth column, 30 year final maturity
13 and you can see there the price you're paying is greater because the
14 interest rates are higher after 30 years so that's what you pay and
15 you've got to decide what to do. That's your decision. We work on
16 these, not illegal and not immoral and it's legitimate and you have to
17 make the decision about what is best for your people. New York City
18 had to spend some money for infrastructure for the deficit. South
19 Carolina it's a healthcare trust plus the tobacco part of the state.
20 Louisiana the same reason for healthcare. So it's a policy decision.
21 So if we're going to do this, we would like to get going in your
22 wisdom if you want to proceed.

23 SENATOR HAWKINS: Any questions?

24 MR. WATKINS: If you put out – I think you were
25 talking about two basis points –

26 MR. COBBS: You're talking about 25 years, 685.

27 MR. WATKINS: And you were saying that California
28 was paying –

29 MR. COBBS: 210, it's based on what the market is.
30 That seems a little high but I'm not sure you can get that much, I think
31 that would be tops. The next page.

32 SECRETARY SCHEWEL: The haircut, the haircut
33 sheet –

34 MR. COBBS: The reduction on, up front what you get
35 up front.

36 SECRETARY SCHEWEL: I understand. My question
37 is, is all the haircut essentially incurred between years 2003 and 2017?
38 It looks to me like it is.

1 MR. COBBS: Sure, because the further you get out, the
2 less effective discount.

3 SECRETARY SCHEWEL: I guess my only point is that
4 sort of when you look at the MPV assuming you're going to receive
5 all the revenue, 218 and 227, it looks like for example, looking at the
6 first column taking 238 million haircut, 945 MPV. What you're doing
7 is taking a 238 million haircut on the first 17 years of revenue.

8 MR. COBBS: On the right-hand side, you're getting
9 money every year and over here you're getting money up front and
10 you assume the turbo is going to start paying out. The turbo is paid
11 off and then you start picking up money again.

12 SECRETARY SCHEWEL: My only point is the same
13 sort of slightly screwy assumption that, which is that you value
14 securitization as if you're going to receive the money in the out years
15 whereas if you're going to receive money in the out years you would
16 secure that in the first place. I think that it's sort of in a way,
17 understates the costs.

18 MR. COBBS: I understand.

19 MR. QUERY: It understates it Mr. Secretary it
20 understates it in one sense but at the same time you're going over a
21 shorter period so actually the haircut will be less. If you did the same
22 PV number and looked at the MSA payments over a 50-year span, the
23 PV costs could end up being higher because you discounted over a
24 longer period. To some extent the time period you're looking over
25 can be somewhat arbitrary. You've got to pick the time horizon in
26 which you want to look and it's one of the difficulties of trying to
27 measure this haircut this way.

28 SECRETARY BENNETT: You're trying to quantify
29 that and that's almost beyond our ability to do over a long term. In
30 reality it seems to me that the market has a view as to how much risk
31 there is associated with securitizing the payments. One of the reasons
32 for the turbo is that reduces their risk and their exposure. So it's the
33 catastrophic risk that you're really avoiding, a large class action
34 settlement fundamentally changes the economics of the market and
35 that's the risk.

36 SENATOR HAWKINS: The presentation has been
37 excellent. Are there any other questions? I note that the house
38 members are not present but we have a majority and we need to move

1 on with this.

2 MR. COBBS: If you have any other questions, I'll be
3 glad to answer them or provide any other information you need.

4 SENATOR HAWKINS: Do you have any
5 recommendations?

6 MR. COBBS: I think 80/20 is probably a good mix.
7 Twenty percent taxable gives you some flexibility on your investment.
8 I think 25 years may be better than 30.

9 SENATOR HAWKINS: We have to make some
10 fundamental decisions tonight. The first decision is on the question of
11 securitization. We should have a unanimous vote to securitize. We
12 have new information, new risk factors and other things involved. Is
13 there a motion to continue the discussion on securitization? It's been
14 moved and seconded that we continue the discussion on securitization.
15 All those in favor say aye (aye). Opposed (no response).

16 SECRETARY SCHEWEL: Mr. Chairman, I move we
17 securitize a 100 percent 80/20 tax exempt taxable split and 25 year
18 maturity.

19
20 NOTE: Motion is seconded.

21
22 SENATOR HAWKINS: That's 80/20 25 years.
23 Everyone understand the motion and discussion? Is there anyone that
24 doesn't understand the position we're taking? Because once we do
25 this, and we give the okay to do this, then cash registers start ringing
26 on our obligation throughout the various groups and we need to
27 understand that as well.

28 SENATOR WAMPLER: Mr. Chairman, I don't know
29 about the members of the House but I made a pass through the
30 chamber while they were negotiating the budget and I believe there
31 was a general consensus 80/20 was the appropriate split and the length
32 and number of years was not discussed but there was a general
33 consensus of the 80/20 split.

34 SENATOR HAWKINS: My understanding is that most
35 people understand what we're talking about. We operate by motion.

36 MR. WALKER: Will this include '03 or '04?

37 SENATOR HAWKINS: '04.

38 MR. WALKER: Can you tell me why you voted for 25

1 years instead of 30?

2 SECRETARY SCHEWEL: It seems to me that the
3 haircut and the extra five years, basically it's \$88 million of proceeds
4 that you would receive under the MSA for that five year period but
5 the portion of that falls to the bottom line. It's about 25, a third of. It
6 seems to me that is a significant haircut. On the other side of the
7 argument, we're already substantially discounted the likelihood we're
8 going to receive the payment and I think we have to reach a
9 conclusion we're counting on receiving any of that years funds. If
10 we're not counting on receiving any of it, receiving \$25 million of it is
11 a lot better than none so I think there's good reasonable argument on
12 either side.

13 MR. OWEN: If you're able to put that \$25 million into
14 your jobs and interest and if we didn't touch it until year 17 at five
15 percent, you're talking about compounding. So when you consider
16 the interest and the time versus \$25 million in your pocket.

17 SECRETARY SCHEWEL: Part of the reason I put it in
18 the motion to talk about it so I think that's a very, or something we
19 should discuss.

20 SENATOR HAWKINS: Well what Claude just said,
21 he's probably had more experience in the tobacco industry than
22 anyone at this table and understands the financing better than anyone.
23 Any comments on the 25 or 30 years.

24 MR. OWEN: Well, I would agree with what Secretary
25 Schewel said about the probability of getting that money in year 17 or
26 18 under the turbo that you're giving up. It took three decades for the
27 participating manufacturers to drop in the United States mid 60's to
28 90's. I know another 25 percent has dropped since 1996 and we know
29 the affect that imports are having on them. We know states are doing
30 the taxes and we get a buyout with the federal legislation. I just don't
31 value very highly given the economics of the industry that the money
32 on paper coming down the road to us in year 18 and the 25 million
33 dollars or whatever it is that we can invest at five percent or more over
34 that period of time.

35 SENATOR HAWKINS: Do you recommend or make a
36 motion to 30?

37 MR. OWEN: Well, I'd like to hear from people, I think
38 it's a significant detraction to it. I'd like to hear from Morgan Stanley

1 on that.

2 MR. QUERY: We've tried to give you an indication and
3 in terms of what the impact on the final yield would be stretching out
4 that additional period. While there is some yield give up and we're
5 talking about a differential of about an eighth of a percent if you will,
6 12.5 basis points. In general terms to us, it's that certainty and that's
7 what you're paying for in terms of structure but in terms of market
8 acceptance, market acceptance for the difference in those two
9 structures is relatively the same, it's a question of yield.

10 MR. OWEN: What about the age?

11 MR. QUERY: What would I do?

12 MR. OWEN: I would move to amend the motion to 30.

13 SENATOR HAWKINS: Thirty-year option, does
14 everyone understand, is there any discussion on this? Mr. Secretary,
15 would you want to restate your motion?

16 SECRETARY SCHEWEL: I would restate my motion
17 that we approve securitization 100 percent of the MSA payments on
18 an 80 percent tax exempt, 20 percent taxable basis with an amendment
19 for a 30 year maturity.

20 SENATOR HAWKINS: Does everyone understand the
21 motion? Is there a second to the motion?

22 MR. OWEN: Second.

23 SENATOR HAWKINS: It's been moved and seconded,
24 any discussion? All in favor say aye (aye) Opposed (no response).

25 MRS. WAGNER: Mr. Chairman, we have a technical
26 resolution that we need to have adopted and the lawyers are here to go
27 through that with you.

28 MR. RICHARDSON: My name is Dave Richardson
29 from McGuire Woods and I'm happy to be here tonight and my
30 partner, Mr. Anderson is with me. In addition to the action that
31 you've just taken, there's a few other things that we need to take a
32 look at in order to get started on the financing. Set aside a sale date
33 and establish squatting rights as has been referred to earlier. If you
34 look at the resolution, the action items are number 1 which is the
35 approval of the long-range plan. The second one is authorization of
36 the transfer of existing funds that are with the Commission into the
37 securitization fund. The reason for doing that, it doesn't change the
38 ultimate use of the funds. The money that is set aside and is being

1 paid, the first quarter of this year, are going to be used for the same
2 purposes. The reason to do that is essentially equity that's going into
3 the endowment fund which allows you to treat it as if it is a taxable
4 bonds without limitation. It's buying more flexibility and on the
5 80/20 split there's also the funds that are currently on hand and will be
6 on hand between now and closing.

7 SENATOR HAWKINS: Do we still have control of
8 those funds?

9 MR. RICHARDSON: Yes.

10 SENATOR HAWKINS: Are they obligated in anyway?

11 MR. RICHARDSON: We're going to the silos into the
12 fund.

13 SENATOR HAWKINS: Like changing the name of the
14 account?

15 MR. RICHARDSON: Right.

16 SENATOR HAWKINS: Any questions about that?

17 MR. WATKINS: Are we going to take the 2000 or this
18 years funds securitize those or are we going to wait and start
19 securitizing funds next year?

20 SENATOR HAWKINS: It's my understanding from the
21 statement that these monies are being used as the foundation and seed
22 money for next years' securitization. This is not securitized.

23 MR. WATKINS: Are you talking about securitizing the
24 2003 payments or are you starting in 2004?

25 SENATOR HAWKINS: 2004.

26 SECRETARY BENNETT: Mr. Chairman, that might
27 seem like a technical question but it's really executive director
28 transferring funds that are on deposit with the treasury. Unless I'm
29 mistaken, I don't think Carthan moves money around. You may
30 direct or authorize the executive director to tell someone to do it but I
31 really think it's either the treasury or the Comptroller.

32 MR. RICHARDSON: That's fine.

33 SECRETARY BENNETT: I believe it's the Treasurer
34 unless Carthan has a key that I don't know about.

35 MRS. WASS: The amounts authorized by the Executive
36 Director.

37 SECRETARY BENNETT: That's fine too, I didn't want
38 to get us into a problem.

1 SENATOR HAWKINS: Is the secretary offering an
2 amendment?

3 SECRETARY BENNETT: It's normally the Treasurer.

4 SENATOR HAWKINS: Let's go through this one more
5 time to make sure we all understand. This is a technical transfer of
6 monies to give the base support for the securitization by having funds
7 in place and people can identify where there at and which are
8 available and in place for this project.

9 MRS. WASS: This is basically, we're securitizing 2004
10 and beyond and to help buy us a little bit of flexibility, we're taking
11 the cash from 2003 and depositing it into the endowment to leave the
12 proceeds from the sale for the 2003 capital expenditures.

13 SENATOR HAWKINS: Any questions?

14 SECRETARY BENNETT: The funds are actually
15 established in the, all we're doing is directing the Comptroller to
16 move the money from one part to another part. So I would make a
17 motion, Mr. Chairman, number two that we provide the Executive
18 Director authorization to request the Comptroller to transfer the funds.

19 SENATOR HAWKINS: Is there any discussion on that?
20 Is there a second to that motion? Alright, it's been moved and
21 seconded, any discussion? All in favor aye (aye) Opposed (no
22 response).

23 MR. RICHARDSON: There's a Memorandum of
24 Understanding –

25 MR. ANDERSON: The only thing that I would mention
26 is that once that equity is put into the endowment, it does become
27 subject, as all the funds in the endowment are to the endowment
28 spending rules. Every year we can spend the earnings off the
29 endowment plus ten percent of the endowment corpus. The amounts
30 are structured as such that the program amounts can be paid out of the
31 endowment.

32 MR. WATKINS: The amounts we've already voted for
33 education this year are affected or are not?

34 MRS. WASS: That chart that showed the cash in 2003
35 and 2004, that's why the amounts are higher. We're going to be
36 paying more this year.

37 MR. RICHARDSON: We're trying to find more taxable
38 bond flexibility without changing the mix of 80/20. Number three

1 addresses the Memorandum of Understanding. The Commission will
2 enter into a Memorandum of Understanding with the Treasurer and
3 the Treasury Board regarding various administrative matters that need
4 to be taken care of that the Treasury will handle. We need an
5 authorization for that to take place. Number four just stresses the plan
6 of finance and percentages and we'll plug those numbers in. Number
7 five is the recognition that although the recommendation has been
8 made by the Commission, that market conditions dictate changes to
9 that and ultimately there may be some variation to the ultimate result
10 of financing. Number six addresses the costs that you all talked about
11 earlier if the transaction does not go forward and would authorize
12 those payments to be made. Number seven authorizes the Executive
13 Director and Chairman to sign the necessary documents that will
14 enable us to go forward with the securitization. What we're trying to
15 do here in one fall swoop is to get the approval that we need in order
16 to get us to the rating agencies and get us to market without bringing
17 the entire Commission back together again because according to the
18 schedule the time you meet again will be April.

19 MR. CURRIN: Mr. Chairman, do we need a roll call?

20 SENATOR WAMPLER: The Chairman stepped out for
21 a minute. Unless anyone prefers otherwise, unless anyone has any
22 other guidance, I prefer a roll call for the record.

23 MR. WATKINS: If we approve this whole thing, do we
24 do the long-range plan later?

25 SENATOR WAMPLER: The action the Commission
26 took previously was to receive the report and by receiving the report
27 we have accepted that as general guidelines.

28 MR. WATKINS: I'm asking for legal guidance.

29 SENATOR WAMPLER: Tucker, let me say something.
30 This is on the financial transaction and that question probably needs to
31 be addressed to the Commission's counsel, the Attorney General. I
32 would say we met the term – Frank.

33 MR. FERGUSON: Give me the question again.

34 MR. WATKINS: Does this document give approval to
35 the long-range plan, does that fix that long-range plan?

36 MR. FERGUSON: No, I think it's fixed as approved
37 tonight. The long range plan that definition, that's just a plan. The
38 document, I guess attested to by the Secretary, if there is such a

1 creature, it should be the Executive Director.

2 SENATOR HAWKINS: I understand for the record we
3 need to take a roll call on the securitization? The question is on the
4 securitization issue, should we securitize the money?

5 MR. RICHARDSON: The action we need is a motion to
6 adopt the resolution as it has been amended.

7 SECRETARY SCHEWEL: So moved.

8 SENATOR PUCKETT: Second.

9 SENATOR HAWKINS: It's been moved and seconded.
10 Call the roll.

11 MR. CURRIN: Mr. Arthur?

12 MR. ARTHUR: Aye.

13 MR. CURRIN: Mr. Banner?

14 MR. BANNER: No response.

15 MR. CURRIN: Secretary Bennett?

16 SECRETARY BENNETT: Aye.

17 MR. CURRIN: Mr. Bryant?

18 MR. BRYANT: Aye.

19 MR. CURRIN: Delegate Byron?

20 DELEGATE BYRON: No response.

21 MR. CURRIN: Mr. Courter.

22 MR. COURTER: Aye.

23 MR. CURRIN: Delegate Dudley?

24 DELEGATE DUDLEY: No response.

25 MR. CURRIN: Mr. Fields?

26 MR. FIELDS: Aye.

27 MR. CURRIN: Mr. Hite?

28 MR. HITE: Aye.

29 MR. CURRIN: Delegate Hogan?

30 DELEGATE HOGAN: No response.

31 MR. CURRIN: Mr. Hopkins?

32 MR. HOPKINS: Aye.

33 MR. CURRIN: Delegate Johnson?

34 DELEGATE JOHNSON: No response.

35 MR. CURRIN: Delegate Kilgore?

36 DELEGATE KILGORE: No response.

37 MR. CURRIN: Mr. Leigh?

38 MR. LEIGH: No response.

1 MR. CURRIN: Mr. Mayhew?
2 MR. MAYHEW: Aye.
3 MR. CURRIN: Mr. Montgomery?
4 MR. MONTGOMERY: Aye.
5 MR. CURRIN: Mr. Owen?
6 MR. OWEN: Aye.
7 MR. CURRIN: Senator Puckett?
8 SENATOR PUCKETT: Aye.
9 MR. CURRIN: Senator Ruff?
10 SENATOR RUFF: Aye.
11 MR. CURRIN: Secretary Schewel?
12 SECRETARY SCHEWEL: Aye.
13 MR. CURRIN: Mr. Stallard?
14 MR. STALLARD: Aye.
15 MR. CURRIN: Mr. Taylor?
16 MR. TAYLOR: Aye.
17 MR. CURRIN: MS. TERRY?
18 MS. TERRY: Aye.
19 MR. CURRIN: Mr. Thompson?
20 MR. THOMPSON: No response.
21 MR. CURRIN: Mr. Walker?
22 MR. WALKER: Aye.
23 MR. CURRIN: Senator Wampler?
24 SENATOR WAMPLER: Aye.
25 MR. CURRIN: Mr. Watkins?
26 MR. WATKINS: Aye.
27 MR. CURRIN: Mr. West?
28 MR. WEST: No response.
29 MR. CURRIN: Mr. Williams?
30 MR. WILLIAMS: No response.
31 MR. CURRIN: Delegate Wright?
32 DELEGATE WRIGHT: No response.
33 MR. CURRIN: Mr. Chairman?
34 SENATOR HAWKINS: Aye. Thank you all. I think a
35 point of clarification in the course of negotiation and discussions on
36 securitization, we're having ongoing discussions with the Executive
37 on how to proceed. The Governor has requested and I think rightly so
38 that we put some money in our budget dealing with our undertaking to

1 make sure we have a foundation in place for the long-range plan.

2 SECRETARY BENNETT: Mr. Chairman, the only point
3 is that he didn't want to hold up the deal but he wanted a chance to
4 discuss with you all the long range plan so what he suggested in his
5 office when you all were sitting there is to include some language in
6 the budget to provide for his approval of the plan and basically let the
7 securitization go forward on the presumption that we'll all work out
8 the details of the plan.

9 SENATOR HAWKINS: To give a certain amount of
10 security to make sure that what we do is fundamentally sound and a
11 reasonable request. That's an ongoing thing for your information.
12 One other thing before we close, we're starting negotiations on E58
13 by putting a foreperson in place this year to start the partnership with
14 the various entities. The bill I drafted created more problems than it
15 solved and I withdrew the bill. We're starting from scratch in
16 negotiations and we've gotten some people's attention like Verizon,
17 the cable people will talk to us now about what they plan the overall
18 structure and we'll work out the details as far as any partnership.

19 MR. OWEN: Before we leave the securitization
20 discussion, you're talking about a securitization committee, I would
21 like to compliment Stephanie Wass and her team and Treasurer
22 Wagner and her team and Senator Wampler's Committee for all the
23 preliminary work that's been done. I think it's a great effort and a
24 great result for us.

25 SENATOR HAWKINS: We have a good team in place
26 and thank you Secretary Wagner, thank you for your work and our
27 staff, that goes without saying. We have a great staff.

28 Any other thing to come forward before we close?
29 Alright, we've got these figures we're handing out and these are raw
30 figures based on all the monies that have been spent. As you go
31 through these none of the indemnification money has been added in
32 here. When we added indemnification monies in you will find certain
33 counties like Pittsylvania County, Halifax, Mecklenburg, large
34 producers of tobacco. We have put \$100 and some million dollars
35 into tobacco communities. And also in the discussion there is a
36 tendency among some of our local government people to look at this
37 as an entitlement. This is not an entitlement, these monies are
38 assigned to this Commission for us to make decisions as far as the

1 distribution of monies. Localities are not entitled to anything unless
2 the Commission decides to do so. We need for all our communities to
3 understand that. Any other comments before we adjourn?

4 MR. CURRIN: Mr. Chairman, in your packets we've
5 given you some future meeting dates of the Commission; April, July
6 and October and we have the location and the dates on that. There
7 may be a need because Virginia Tech has their report done. I would
8 possibly recommend Mr. Chairman that there may be a need for the
9 Commission to meet in March to review and receive that report.

10 SENATOR HAWKINS: We have a large amount of
11 time between those dates but that lapse of time allows itself and
12 creates sometimes misinformation floating around. Would it be
13 helpful to have more meetings or more correspondence from the
14 Commission. What can we do to make the process better, more
15 meetings?

16 MR. CURRIN: Mr. Chairman, this is a rather large
17 Commission, since so much work is done by the Committee, maybe
18 the committees need to meet more.

19 SENATOR HAWKINS: We need to make sure we keep
20 an open dialogue between all the members so we understand what is
21 taking place and we can work that out. The Committees need to work
22 on these different areas.

23 MS. TERRY: It would be helpful if we all could count
24 on getting notices of all the Committee meetings and we also might
25 have an interest just in what's going on with certain subcommittees as
26 far as the subject matter area. Would there be a problem Mr.
27 Chairman, if some kind of notice, when the Committees are meeting
28 and maybe set up some type of telecommunication so that a person
29 could just listen.

30 SENATOR HAWKINS: That's a strong possibility MS.
31 TERRY. We might be able to use those facilities in some of these
32 Committee meetings.

33 MS. TERRY: When these Committees meet, if we're not
34 a member of the Committee or we don't have a vote, at least we could
35 listen in and we'll know what they've been talking about. If we knew
36 for example a certain committee was meeting at a certain time, maybe
37 there were call in numbers, we could just listen and know what was
38 going on.

1 SENATOR HAWKINS: I think an informational
2 meeting certainly would be helpful.

3 MR. CURRIN: Mr. Chairman, everybody on the
4 Commission is notified about the Committee meetings along with the
5 general public.

6 MR. HITE: I think all the members should be notified
7 too.

8 SENATOR HAWKINS: With the new structure of the
9 Committees and with more balanced representation and the number of
10 people on these Committees now, hopefully we can with more
11 structure make representations to the full body. Anything else to
12 come before the Commission? Going once, going twice.

13
14 PROCEEDINGS CONCLUDED
15

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17
18 CERTIFICATE OF THE COURT REPORTER
19

20
21 I, Medford W. Howard, Registered Professional Reporter
22 and Notary Public for the State of Virginia at large, do hereby certify
23 that I was the court reporter who took down and transcribed the
24 proceedings of the Virginia Tobacco Indemnification and Community
25 Revitalization Commission, full Commission meeting when held on
26 Thursday, February 6, 2003 at 6:00 o'clock p.m. in the John Marshall
27 Hotel, Marshall Room in Richmond, Virginia 23219.

28 I further certify this is a true and accurate transcript to the
29 best of my ability to hear and understand the proceedings.

30 Given under my hand this 15th day of February 2003.

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Medford W. Howard

5

Registered Professional Reporter

6

Notary Public for the State of Virginia at Large

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MY COMMISSION EXPIRES: October 31, 2006

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